



## TO INCORPORATE OR NOT

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There are several reasons why individuals or partnerships decide to incorporate their businesses. The main advantage of incorporation is that it provides limited liability to the shareholders. There are also several tax advantages associated with incorporation, these include the tax reliefs available to corporates only. These include:

- Start-up exemption for corporation tax for new business;
- Research and development (R&D) credits for business engaged in qualifying R&D activity; and
- Intangible Asset Scheme for intellectual property (IP) acquired by corporates.

Being a corporate also provides more flexibility in terms of succession planning, pension planning and exiting shareholders when compared to the traditional sole trade or partnership model.

## SUCCESSION PLANNING

In terms of succession planning, shares of different classes can be issued to shareholders with different rights. This can potentially provide a more economic mechanism of participation in business for new shareholders.

In the traditional partnership model, new partners need to obtain funding to purchase a share of the business. A corporate entity is more flexible in this regard, as it allows individuals become shareholders without the need to obtain large personal loans to finance their acquisition of part of a business.

## PENSION PLANNING

Corporate pensions provide more flexibility compared to traditional personal pension schemes and PRSAs in terms of funding.

## EXIT PLANNING

The existing reserves of the company can be used to repurchase an existing shareholder's shares. This can be done by means of a share buyback, which can provide a useful means of funding the exit of a shareholder.

Incorporation therefore allows a business to admit and exit new shareholders far easier than the traditional sole trader or partnership mould.

## HOW TO INCORPORATE

There are two potential mechanisms to incorporate a business. These are:

- A straight sale of assets, including goodwill, to a corporate where the consideration for the assets is left outstanding by means of director's loan; or

- Shares issued by the company in return for the assets transfers and relief under Section 600 is claimed from capital gains tax (CGT). This relief defers the CGT payable by reducing the base cost of the shares.

To decide which mechanism of incorporation is optimal depends on the rationale for incorporation. Section 600 relief may not be favourable, for example, where valuable land and buildings have to be transferred to avail of the relief.

## THE DISADVANTAGES

There are also disadvantages of incorporating. They include the greater level of compliance associated with operating through a company and also, the greater level of warranties and indemnities that need to be provided on sale of the shares in the corporate entity. Submissions to scope may also be required to remain on Class S PRSI, where the shareholders retain less than 50% of the overall shareholding.

In summary, incorporating a business provides greater legal protection and flexibility for individuals. Care must be exercised to ensure that the timing of incorporation is correct and that all available reliefs are availed of to mitigate potential taxes. Consideration should also be given to all taxes including CGT, VAT, income tax and stamp duty before incorporating the business.